REPORT OF THE

ASSOCIATION FINANCIAL EXAMINATION OF

SHELTER GENERAL INSURANCE COMPANY

AS OF

DECEMBER 31, 2001

STATE OF MISSOURI

DEPARTMENT OF INSURANCE

JEFFERSON CITY, MISSOURI

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Columbia, Missouri
September 17, 2003

Chairman of Financial Condition (EX4) Subcommittee
Southeastern Zone Secretary
Honorable Alfred W. Gross, Commissioner
Virginia Bureau of Insurance

Midwestern Zone Secretary
Jim Poolman, Commissioner
North Dakota Department of Insurance

Honorable Scott B. Lakin, Director
Missouri Department of Insurance
301 West High Street, Room 530
Jefferson City, Missouri 65101

Gentlemen:

In accordance with your financial examination warrant, a full scope association financial examination has been made of the records, affairs and financial condition of

Shelter General Insurance Company

hereinafter referred to as such, as Shelter General, or as the Company. Its administrative office is located at 1817 West Broadway, Columbia, Missouri 65218, telephone number 573-445-8441. This examination began on November 4, 2002, and concluded on the above date.

SCOPE OF EXAMINATION

Period Covered

The prior full scope association financial examination of Shelter General was made as of December 31, 1998, and was conducted by examiners from the State of Missouri representing the Midwestern Zone of the National Association of Insurance Commissioners (NAIC), with no other zones participating.

The current full scope association financial examination covered the period from January 1, 1999, through December 31, 2001, and was conducted by examiners from the State of Missouri, representing the Midwestern Zone of the NAIC, with no other zones participating.

This examination was conducted concurrently with the examinations of the Company's parent, Shelter Mutual Insurance Company (Shelter Mutual), and its affiliates, Shelter Life Insurance Company (Shelter Life), and Shelter Reinsurance Company (Shelter Reinsurance). Shelter Mutual and its insurance subsidiaries are collectively referred to as the Shelter Insurance Companies in this report.

This examination also included the material transactions and/or events occurring subsequent to the examination date, which are noted in this report.

Procedures

This examination was conducted using the guidelines set forth in the Financial Condition Examiners Handbook of the NAIC, except where practices, procedures and applicable regulations of the Missouri Department of Insurance (MDI) and statutes of the State of Missouri prevailed.

The examiners relied upon information supplied by the Company's independent auditor, PriceWaterhouseCoopers, LLP, of St. Louis, Missouri, for its audit covering the period from January 1, 2001, through December 31, 2001. Information relied upon included attorney letters, tests of controls, and narrative descriptions of processes and controls.

Comments - Previous Examination

The previous financial examination of Shelter General was conducted by the MDI for the period ending December 31, 1998. Listed below are the comments, recommendations, and notes from the previous examination report, the Company's response, and the findings in the current examination.

Fidelity Bond

Comment: It was recommended that the Company should obtain a minimum of $700,000 of fidelity coverage to cover employees for dishonest acts in the normal course of business as recommended by the NAIC guidelines for the protection of its assets.

Company's Response: The Company stated that the fidelity bond coverage had been obtained as recommended.

Current Findings: The Company currently has a financial institution bond that provides fidelity coverage in excess of the minimum level recommended by the guidelines of the NAIC. Refer to the Fidelity Bond and Other Insurance section of this report for further details.

Reinsurance

Comment: It was noted that several of Shelter General's ceded reinsurance contracts had insolvency clauses, which allow for the reinsurer to pay the insured directly in the event of insolvency. Such provisions in insolvency clauses were not allowed by Missouri Regulation 20 CSR 200-2.100 (11)(A) (Credit for Reinsurance). It was recommended that the Company should review and update the insolvency clauses in its reinsurance agreements.

Company's Response: The Company stated that its ceded reinsurance contracts had been reviewed and changes were being made to have them conform with Missouri Regulation 20 CSR 200-2.100 (11)(A).

Current Findings: The insolvency clause provisions of Missouri Regulation 20 CSR 200-2.100 (11) (A) were superceded by revisions made to Section 375.246 RSMo (Reinsurance Credits), effective August 28, 2002. This statute now provides for instances in which payments from a reinsurer may be made directly to an insured. The insolvency clauses for the agreements that were reviewed during the examination were found to be in compliance with Missouri statutes and regulations.

Accounts and Records

Comment: It was recommended that the Company should maintain claim files for the year in which the claim is closed plus three calendar years, in accordance with Section 374.205 RSMo (Examination of Insurers).

Company's Response: The Company stated that its retention policy and practices were revised to conform with Section 374.205 RSMo.

Current Findings: Missing claim files were discovered during a sample testing of paid claim files. Refer to the Accounts and Records section of this report for further information.

HISTORY

General

Shelter General was incorporated and commenced business on November 12, 1957. The Company was originally named Countryside Casualty Company. The Company's name was changed to Shelter General Insurance Company on July 1, 1981. The Company operates as a stock property and casualty insurer under the insurance laws of Chapter 379 RSMo (Insurance Other Than Life).

Capital Stock

Shelter General is owned 100% by Shelter Mutual. The Company is authorized to issue 1,250,000 shares of common stock with a par value of $1 per share. As of December 31, 2001, all 1,250,000 shares were issued and outstanding for a total capital stock balance of $1,250,000.

Dividends

The Company paid a $3,000,000 dividend to Shelter Mutual in 2000. No dividends or cash distributions were paid or declared during 1999 or 2001.

Management

The management of the Company is vested in a Board of Directors that are appointed by the sole shareholder, Shelter Mutual. The Company's Articles of Incorporation and Bylaws specify that the number of directors shall be nine. The Board of Directors appointed and serving, as of December 31, 2001, were as follows:

Name and Address	Principal Occupation and Business Affiliation
James A. Offutt Osage Beach, MO	Chairman, Retired Executive Shelter Insurance Companies
Robert W. Maupin% Columbia, MO	Vice Chairman, Retired Executive Shelter Insurance Companies
Raymond E. Jones Columbia, MO	Executive Vice President and Secretary Shelter Insurance Companies
H. Marshall Chatfield Columbia, MO	Retired Executive Kansas City Life Insurance Company
Ann K. Covington Columbia, MO	Attorney / Partner Bryan Cave, LLP
John D. Duello Rocheport, MO	President and Chief Executive Officer Shelter Insurance Companies
Andres Jimenez Madrid, Spain	Vice President and Chief Executive Officer MAPFRE Re Compania de Reaseguros, S.A.
John W. Lenox* Columbia, MO	Retired Executive Shelter Insurance Companies
Barry L. McKuin Morrilton, AR	President Morrilton Area Chamber of Commerce

* Mr. Lenox died in November 2002 and was replaced by Don A. McCubbin in April 2003
% Mr. Maupin retired in April 2003 and was replaced by Dr. Gerald Brouder in May 2003

Committees

The Bylaws require an Executive and Compensation Committee and an Audit Committee of the Board of Directors. The Bylaws also allow for other committees to be appointed by the Board of Directors as needed. An Investment Committee was in operation during and subsequent to the examination period. As of December 31, 2001, the members of each committee were as follows:

Executive and Compensation Committee
Robert W. Maupin, Chairman
J. Donald Duello
H. Marshall Chatfield
James A. Offutt
Ann K. Covington

Audit Committee
Barry L. McKuin, Chairman
Ann K. Covington
H. Marshall Chatfield

Investment Committee
J. Donald Duello, Chairman
Raymond E. Jones
Thomas Fischer
John W. Lenox
Robert W. Maupin
James A. Offutt
H. Marshall Chatfield

Officers

The officers elected by the Board of Directors and serving, as of December 31, 2001, were as follows:

John D. Duello	President and Chief Executive Officer
Raymond E. Jones	Executive Vice President and Secretary
Robert T. Cox #	Executive Vice President and General Counsel
Don A. McCubbin	Executive Vice President - Underwriting
Jerry L. French	Vice President, Treasurer and Assistant Secretary
Max T. Dills @	Vice President – Actuarial
Thomas N. Fischer	Vice President – Investments
Gary L. Ford	Vice President – Planning and Research
William C. Keithley	Vice President – Information Services
Ricky L. Means **	Vice President – Claims
John D. Moore	Vice President – Marketing
Joe L. Moseley	Vice President – Public Affairs
Gary D. Myers ***	Vice President – Administration
Donald H. Northway	Vice President – General Services
L. Gerald Brooks	Assistant Treasurer

Robert T. Cox resigned effective March 1, 2002 and was replaced by Randa C. Rawlins on April 15, 2002. Ms. Rawlins was appointed as General Counsel only.

@ Max T. Dills was elected as Vice President – Administration on February 21, 2002. S. Daniel Clapp was elected Vice President – Actuarial on that date also.

** Ricky L. Means was elected Vice President – Underwriting on February 21, 2002. Patrick D. Gruber was elected Vice President – Claims on that date also.

*** Gary D. Myers was elected Executive Vice President on February 21, 2002.

Conflict of Interest

The Company has a policy that requires all officers, directors, and key employees to complete a conflict of interest statement each year. Signed statements of officers and directors were reviewed for the examination period. No significant exceptions were noted.

Corporate Records

A review was made of the Articles of Incorporation and Bylaws for the examination period. There were no amendments or changes to the Articles of Incorporation during the period under examination. The Bylaws were amended in April 2001 to require an Audit Committee to be maintained.

The minutes of the Board of Directors' meetings, committee meetings, and stockholders' meetings were reviewed for proper approval of corporate transactions. In general, the minutes appear to properly reflect and approve the Company's major transactions and events for the period under examination.

Acquisitions, Mergers and Major Corporate Events

None.

Surplus Debentures

No surplus debentures were issued or outstanding for the period under examination.

AFFILIATED COMPANIES

<u>Holding Company, Subsidiaries and Affiliates</u>

The Company is a member of an Insurance Holding Company System as defined by Section 382.010, RSMo (Definitions). An Insurance Holding Company System Registration Statement was filed by the parent, Shelter Mutual, on behalf of itself, Shelter General, and its other insurance subsidiaries, for each year of the examination period.

Shelter Mutual, a property and casualty insurer, does not have any stockholders or controlling entity due to its formation as a mutual entity. The Company is ultimately owned by the policyholders of Shelter Mutual. Affiliated insurers that are also owned 100% by Shelter Mutual include Shelter Reinsurance, an international reinsurance company, and Shelter Life, a life insurance company.

Shelter General has partial ownership of the following subsidiaries:

Shelter Financial Services, Inc. (SFS) – A holding company for Shelter Benefits Management, Inc.

Shelter Benefits Management, Inc. (Shelter Benefits) – Provides the human resource function and manages agent and employee benefits for the Shelter Insurance Companies.

Shelter Enterprises, LLC – This is a small entity (only $6.1 million of total assets) that owns property and equipment and derives its income from leasing the assets to affiliates, including Shelter Mutual, and non-affiliates.

Daniel Boone Underwriters, LLC – An insurance broker that places risks from leads generated by agents of the Shelter Insurance Companies. The risks placed are in lines of business that are not written by Shelter Mutual or Shelter General.

Daniel Boone Agency, Inc. – An insurance broker in the same manner as explained for Daniel Boone Underwriters, LLC above, except that this entity operates in Illinois only.

DBU, Inc. – An insurance broker in the same manner as explained for Daniel Boone Underwriters, LLC above, except that this entity operates in Mississippi only.

The operations of the Company's other affiliates are described as follows:

Shelter Financial Corporation (SFC) – A holding company for Shelter Bank.

Shelter Bank – A savings and loan company that sells certificates of deposits, individual retirement accounts, and provides auto loans and mortgage loans. It does not have any demand accounts (checking or savings). Its customers are mainly policyholders of Shelter Mutual and Shelter General, but customers may also come from the general public.

Shelter (UK) Holdings, Ltd. – A holding company for Shelter Dedicated, Ltd. and Commodore Underwriting Agencies, Ltd.

Shelter Dedicated, Ltd. – A Lloyd's of London corporate member that accepts risks for a Lloyd's syndicate. Accepted risks for the policy year from January 1, 2001 through December 31, 2001. Due to the poor experience, no other risks were accepted after 2001. The company is now in run-off with a three-year accounting period ending December 31, 2003.

Commodore Underwriting Agencies, Ltd. (Commodore) – An underwriter for risks taken by Shelter Dedicated, Ltd and other Lloyd's syndicates. As of the first quarter of 2003, the entity has no operations, employees, or significant assets.

Organizational Chart

The following table depicts Shelter General's ownership and holding company system, as of December 31, 2001:

Company	Parent or Controlling Entity	Ownership
Shelter Mutual Insurance Company	Policyholders	100%
Shelter General Insurance Company	Shelter Mutual Insurance Company	100%
Shelter Enterprises, LLC	Shelter General Insurance Company Shelter Life Insurance Company Shelter Reinsurance Company	45% 45% 10%
Shelter Life Insurance Company	Shelter Mutual Insurance Company	100%
Shelter Reinsurance Company	Shelter Mutual Insurance Company	100%
Shelter (UK) Holdings, Ltd.	Shelter Reinsurance Company	100%
Shelter Dedicated, Ltd.	Shelter (UK) Holdings, Ltd.	100%
Commodore UW Agencies, Ltd.	Shelter (UK) Holdings, Ltd.	100%
Shelter Financial Corporation	Shelter Mutual Insurance Company	100%
Shelter Bank	Shelter Financial Corporation	100%
Shelter Financial Services, Inc.	Shelter Mutual Insurance Company Shelter General Insurance Company Shelter Life Insurance Company	79.5% 11% 9.5%
Shelter Benefits Management, Inc.	Shelter Financial Services, Inc.	100%
Daniel Boone Underwriters, LLC	Shelter Mutual Insurance Company Shelter General Insurance Company Shelter Life Insurance Company	40% 40% 20%
Daniel Boone Agency, Inc.	Daniel Boone Underwriters, LLC	100%
DBU, Inc.	Daniel Boone Underwriters, LLC	100%

Intercompany Agreements

The Company's intercompany agreements in effect, as of December 31, 2001, are outlined below.

1. **Type:** Joint Expense Allocation Agreement

   Affiliates: Shelter Mutual, Shelter Life, Shelter Reinsurance, SFS, Daniel Boone Underwriters, LLC, Shelter Enterprises, LLC, Daniel Boone Agency, Inc., DBU, Inc., Shelter Benefits

   Effective: May 19, 1999

   Terms: Each party agrees to pay its direct expenses in instances when each entity's actual usage can be determined. The parties agree to allocate any joint expenses for instances in which the identification and segregation of each entity's actual share is not practically feasible. The allocation methodologies for each category of joint expenses are as follows:

   (1) Personnel – estimated or actual time
   (2) Real Estate – square footage and employee count
   (3) Investment – portfolio value
   (4) Claims Adjustment (applicable to Shelter Mutual and Shelter General only) – incurred losses
   (5) Other Expenses – assets, employee count, or written premium

2. **Type:** Transfer and Assumption Agreement

   Affiliates: Shelter Mutual, Shelter Life, Shelter Benefits

   Effective: May 19, 1999

   Terms: Shelter General and Shelter Life paid $3,124,245 and $636,571, respectively, to Shelter Mutual for the purpose of transferring both companies agent termination pay liabilities. Shelter Mutual transferred certain agent liabilities and employee benefit liabilities totaling $95,223,532, as of May 19, 1999, to Shelter Benefits. The liabilities transferred included agents termination benefits, post-retirement benefits, accrued vacation benefits, and director's retirement plan benefits. In exchange, Shelter Mutual assigned its rights to the $100,223,532 promissory note issued by Shelter Life to Shelter Benefits. Shelter Benefits also issued 500,000 shares of preferred stock, with a total par value of $5,000,000 to Shelter Mutual. Finally, Shelter Benefits agrees to assume future agent liabilities and employee benefit liabilities from Shelter Mutual.

3. **Type:** Tax Allocation Agreement

   Affiliates: Shelter Mutual, Shelter Life, Shelter Reinsurance, SFS, SFC, Shelter Benefits, Shelter Bank

   Effective: No stated effective date. Applicable to 1999 and subsequent tax years.

   Terms: Shelter Mutual will file a consolidated federal income tax return on behalf of itself and its subsidiaries. The tax liability for each company will be the amount that would have been determined on a separate filing basis. The subsidiaries will pay their share of tax payments to Shelter Mutual within 10 days following any tax payments made by Shelter Mutual. Shelter Mutual will refund any amount due to the subsidiaries within 10 days after filing the consolidated return.

Shelter General is a named insured on a general liability insurance policy issued by Shelter Mutual. The policy insures the premises and operations of the Shelter Mutual and all named insureds. Premium for this policy is charged to Shelter General through intercompany allocations under the Joint Expense Allocation Agreement.

Employees of Shelter Mutual perform all functions necessary for the operation of Shelter General. Shelter General does not have a written agreement with Shelter Mutual for the management services and facilities that are provided by Shelter Mutual and the associated costs to be allocated under the Joint Expense Allocation Agreement. The Company is directed to obtain a written agreement with Shelter Mutual, similar to the Management Services and Facilities Agreements that exist between Shelter Mutual and other subsidiaries. Such agreement should be submitted as a Form D filing to the MDI for prior approval in accordance with Section 382.195 RSMo (Transactions Within a Holding Company System).

Intercompany Payments

The following table summarizes the payments made during the exam period, between Shelter General and its affiliates.

		Net Paid / (Received)		
Related Party	Agreement	1999	2000	2001
Shelter Mutual	Joint Expense Allocation	$16,783,813	$15,448,232	$15,116,456
Shelter Mutual	Tax Allocation	322,557	1,911,693	(521,358)
Shelter Benefits	Transfer and Assumption	105,884	(3,146)	(49,815)
TOTAL		$17,212,254	$17,356,761	$14,545,283

FIDELITY BOND AND OTHER INSURANCE

The Shelter Insurance Companies are named insureds on a financial institution bond. The bond provides employee fidelity coverage with a liability limit of $2,500,000 and a $50,000 deductible. This level of coverage complies with the suggested minimum amount of fidelity insurance according to NAIC guidelines.

The Shelter Insurance Companies are also named insureds on the following insurance policies: property, general liability, umbrella excess liability, automobile physical damage and liability, aircraft physical damage and liability, workers compensation and employers liability, computer crime, kidnap and ransom / extortion, and earth movement.

PENSION, STOCK OWNERSHIP AND INSURANCE PLANS

Shelter General does not have any direct employees or agents. Employees and agents of the parent, Shelter Mutual, perform all functions necessary for the operation of Shelter General. There is no written agreement between the Company and Shelter Mutual for this arrangement, as described in the Intercompany Agreements section of this report. Shelter General reimburses

Shelter Mutual for an allocated share of the payroll and benefits costs of the employees that provide services, pursuant to a Joint Expense Allocation Agreement.

A variety of standard benefits are provided to the Shelter Mutual employees and agents. These benefits include, but are not limited to, the following: medical insurance, dental insurance, life insurance, personal accident insurance, disability insurance, sick leave, and tuition reimbursement. Employees are also provided with a defined benefit pension plan and a 401(k) savings and profit sharing plan. Certain highly compensated employees are provided with a Supplemental Employee Retirement Plan (SERP).

STATUTORY DEPOSITS

Deposits with the State of Missouri

The funds on deposit with the Missouri Department of Insurance as of December 31, 2001, were sufficient to meet the capital deposit requirements for the State of Missouri in accordance with Section 379.098 RSMo (Securities Deposit). The funds on deposit as of December 31, 2001, were as follows:

Type of Security	Par Value	Fair Value	Statement Value
U.S. Treasury Notes	$2,000,000	$2,087,500	$1,944,719

Deposits with Other States

The Company also has funds on deposit with other states. Those funds on deposit as of December 31, 2001, were as follows:

State	Type of Security	Par Value	Fair Value	Statement Value
Arkansas	U.S. Treasury Notes	$300,000	$314,907	$310,764
Louisiana	U.S. Treasury Notes	100,000	104,969	103,588
Oklahoma	U.S. Treasury Notes	300,000	314,907	310,764
Total		$700,000	$734,783	$725,117

INSURANCE PRODUCTS AND RELATED PRACTICES

Territory and Plan of Operation

Shelter General is licensed as a property and casualty insurer by the Missouri Department of Insurance under Chapter 379 RSMo (Insurance Other than Life). The Company is licensed and writes business in Missouri and 12 other Midwestern states, as follows:

Arkansas	Indiana	Kentucky	Nebraska
Colorado	Iowa	Louisiana	Oklahoma
Illinois	Kansas	Mississippi	Tennessee

In addition, the Company is a licensed reinsurer in New Hampshire and South Carolina. However, no business was assumed during the examination period with these licenses.

Written premiums in four states (Arkansas, Missouri, Oklahoma, and Tennessee) accounted for 64% of the total direct written premiums in 2001. The major lines of business for Shelter General, based upon 2001 net written premiums, are as follows:

Line of Business	Percentage of Total Net Written Premiums
Private Passenger Auto Liability	51.5%
Commercial Auto Liability	6.8%
Auto Physical Damage	35.6%
All Other	6.1%
Total	100.0%

The parent, Shelter Mutual, generally writes all homeowners and preferred auto risks, while Shelter General specializes in standard auto risks. There are two states that are exceptions to this plan of operations. A management decision was made to write all new auto business in Illinois and Tennessee through Shelter General in 2001.

The Company's products are marketed by approximately 1,400 captive agents, which also produce business for the parent, Shelter Mutual, and two affiliates, Shelter Life and Shelter

Bank. Shelter Mutual also has a marketing staff that uses various methods of advertising and direct mailings to promote the products of Shelter General and its affiliates.

Policy Forms & Underwriting;
Advertising & Sales;
Treatment of Policyholders

The Missouri Department of Insurance has a market conduct staff that performs a review of these issues and generates a separate market conduct report. The most recent MDI market conduct examination report was dated April 25, 2002, and covered the period from October 1, 2000 to September 30, 2001. No significant problems were noted from review of this report.

REINSURANCE

General

The Company's premium activity on a direct written, assumed and ceded basis, for the period under examination, is detailed below:

	1999	2000	2001
Direct Business	$89,618,753	$87,130,110	$83,474,341
Reinsurance Assumed	0	0	0
Reinsurance Ceded:			
Affiliates	(569)	(706)	(342)
Non-affiliates	(512,842)	(526,294)	(494,403)
Net Premiums Written	**$89,105,342**	**$86,603,110**	**$82,979,596**

Assumed

The Company does not assume any business, except for involuntary pools and associations.

<u>Ceded</u>

The Company is contingently liable for all reinsurance losses ceded to others. This contingent liability would become an actual liability in the event that an assuming reinsurer fails to perform its obligations under the reinsurance agreement.

Shelter General has limited ceded reinsurance activity due to the auto business that accounts for nearly all of its direct premiums. The policy limits for auto property coverage are retained 100% by the Company except in instances when a catastrophe occurs. The Company only reported ceded loss reserves of $1,261,000, as of December 31, 2001. This amount is for liability risks that are ceded to one reinsurer, Employers Reinsurance Corporation (ERC).

Shelter General and its parent, Shelter Mutual, have an excess reinsurance agreement, originally effective January 1, 1975, with ERC that appears to cover auto liability and general liability risks. The retention appears to be $500,000 or $625,000 per occurrence depending on the amount of loss adjustment expenses. ERC's liability appears to be limited to $4,000,000 in excess of the retention. The reinsured lines of business, the retention, and the reinsurance limits are not clearly defined because of the 44 amendments that have taken place since the inception of the agreement in 1975. The terms of the agreement are subject to interpretation because it is impossible to tie together the disjointed and confusing terminology from all of the amendments and the original body of the agreement together in a coherent manner. It is recommended that this agreement should be restated in its entirety so that the reinsured lines of business, retentions, and limits are clearly defined.

Shelter General and Shelter Mutual have a quota share / excess agreement with ERC, effective October 1, 1985, that covers personal umbrella, personal liability, professional liability, and excess medical expense risks. Shelter Mutual and Shelter General retain 5% of the first $1,000,000 of losses while ERC assumes the remaining 95%. The next $1,000,000 of losses in excess of the first $1,000,000 are ceded 100% to ERC.

Shelter General and Shelter Mutual have a five-layer catastrophe excess of loss agreement, effective January 1, 2001, with several reinsurers. The participation of each reinsurer is defined in an Interest and Liabilities Agreement with each reinsurer. The agreement covers all property risks including auto physical damage. The reinsurance coverages for the combined subject net losses of Shelter Mutual and Shelter General for each layer are as follows:

Layer	Subject Net Losses	Reinsurance %
First	$9,000,000 excess of $14,000,000	95%*
Second	$15,000,000 excess of $23,000,000	95%
Third	$22,000,000 excess of $38,000,000	95%
Fourth	$41,000,000 excess of $60,000,000	95%
Fifth	$15,000,000 excess of $101,000,000	100%

* Reinsurer's participation was only 66.5% for the first layer. Actual reinsurance coverage is 66.5% of 95% or 63.175%.

The catastrophe agreements are renewed each year. Effective with the January 1, 2002 renewal, the reinsurance coverages for the combined subject net losses of Shelter Mutual and Shelter General for each layer are as follows:

Layer	Subject Net Losses	Reinsurance %
First	$10,000,000 excess of $25,000,000	95%
Second	$15,000,000 excess of $35,000,000	95%
Third	$25,000,000 excess of $50,000,000	95%
Fourth	$40,000,000 excess of $75,000,000	95%
Fifth	$20,000,000 excess of $115,000,000	100%

Effective with the January 1, 2003 renewal, the reinsurance coverages for the combined subject net losses of Shelter Mutual and Shelter General for each layer are as follows:

Layer	Subject Net Losses	Reinsurance %
First	$10,000,000 excess of $25,000,000	95%
Second	$15,000,000 excess of $35,000,000	95%
Third	$30,000,000 excess of $50,000,000	95%
Fourth	$40,000,000 excess of $80,000,000	95%
Fifth	$65,000,000 excess of $120,000,000	95%
Sixth	$20,000,000 excess of $185,000,000	100%

As described above, all of Shelter General's reinsurance agreements are joint agreements with Shelter Mutual. Shelter General does not directly pay reinsurance premiums to the reinsurers. Instead, Shelter Mutual makes a single, combined premium payment to the reinsurers on behalf of both companies. Likewise, losses from both companies are combined for determining retentions and coverage amounts. Reinsurance recoveries for combined losses are paid to Shelter Mutual. Shelter General pays an allocated a share of the combined reinsurance premiums to Shelter Mutual and receives an allocated share of loss recoveries from Shelter Mutual as part of the intercompany settlement process. There is no written agreement with Shelter Mutual for this process. The Company is directed to enter into a written agreement with Shelter Mutual for the allocation of reinsurance premiums and loss recoveries in accordance with Section 382.195 RSMo (Transactions Within a Holding Company System). This agreement should be filed with the MDI for prior approval.

ACCOUNTS AND RECORDS

General

The CPA firm, PricewaterhouseCoopers, LLP, of St. Louis, Missouri, issued audited statutory financial statements of the Company for all years in the examination period.

The reserves for losses and loss adjustment expenses were reviewed and certified by Terrence M. O'Brien, FCAS, MAAA, CPCU for all years in the examination period. Mr. O'Brien is employed by PricewaterhouseCoopers, LLP, of Chicago, Illinois.

Claim Files

A statistical sample of claims paid in 2001 was selected from data supporting Schedule P of the Annual Statement for Shelter Mutual and Shelter General. The Company was unable to locate three claim files and several months of research were required to locate other claim files. If the results from this statistical sample was extrapolated to the entire population of paid claims, then the Company would appear to have numerous claim files that are either missing or not filed properly. Section 374.205.2(2) RSMo (Examination of Insurers) requires insurers to maintain claim files for the year in which the claim is closed, plus 3 calendar years. The Company should review its procedures for the filing, maintenance, and retention of claim files and improve these procedures to ensure that all claim files are retained in accordance with the cited law.

FINANCIAL STATEMENTS

The following financial statements, with supporting exhibits, present the financial condition of Shelter General for the period ending December 31, 2001. Any examination adjustments to the amounts reported in the financial statements and/or comments regarding such are made in the "Notes to the Financial Statements." The failure of any column of numbers to add to its respective total is due to rounding or truncation.

There may have been additional differences found in the course of this examination, which are not shown in the "Notes to the Financial Statements." These differences were determined to be immaterial concerning their effect on the financial statements, and therefore, were only communicated to the Company and noted in the workpapers for each individual Annual Statement item.

Assets
as of December 31, 2001

	Assets	Non-Admitted Assets	Net Admitted Assets
Bonds	$96,643,211	$0	$96,643,211
Common Stocks	28,294,466	0	28,294,466
Cash and Short-term Investments (**Note 1**)	5,934,273	0	5,934,273
Other Invested Assets	2,858,635	0	2,858,635
Agents' Balances or Uncollected Premiums:	7,734,780	0	7,734,780
Bills Receivable, Taken for Premiums	590,787	0	590,787
Reinsurance Recoverables on Losses and LAE	850,584	0	850,584
Investment Income Due and Accrued	1,668,643	0	1,668,643
Receivable from Parent, Sub., and Affiliates	95,157	0	95,157
Equities and Deposits in Pools and Assoc.	274,645	136,473	138,172
Agg. Write-Ins for Other than Invested Assets:			
Missouri Affordable Housing Project Fund	1,664,780	0	1,664,780
Miscellaneous Suspense Accounts	1,029	0	1,029
TOTAL ASSETS	**$146,610,990**	**$136,473**	**$146,474,517**

Liabilities, Surplus and Other Funds
as of December 31, 2001

Losses	$ 37,916,451
Loss Adjustment Expenses	6,234,731
Commissions Payable	1,333,368
Other Expenses	637,305
Taxes, Licenses and Fees	250,060
Federal Income Taxes	5,434,127
Unearned Premiums	19,801,705
Ceded Reinsurance Premiums Payable	15,618
Amounts Withheld or Retained	70,385
Drafts Outstanding	3,421,711
Payable to Parent, Subsidiaries and Affiliates	2,025,243
Aggregate Write-Ins for Liabilities:	
Catastrophe Reserve – Earthquake	209,835
Advance Premium	2,056,442
Premium Deficiency Reserve	74,143
Other Liabilities	310,828
TOTAL LIABILITIES	**$79,791,952**
Common Capital Stock	1,250,000
Unassigned Funds (Surplus)	65,432,565
Surplus as Regards Policyholders	**$66,682,565**
TOTAL LIABILITIES AND SURPLUS	**$146,474,517**

Statement of Income
For the Year Ended December 31, 2001

Premium Earned	**$82,407,761**
DEDUCTIONS:	
Losses Incurred	64,506,172
Loss Expenses Incurred	6,192,800
Other Underwriting Expenses Incurred	20,287,664
Aggregate Write-Ins for Underwriting Deductions	(201,370)
Total Underwriting Deductions	**$90,785,266**
Net Underwriting Loss	**($8,377,505)**
Net Investment Income Earned	7,193,615
Net Realized Capital Gains	1,919,262
Net Investment Gain	**$9,112,877**
Other Income	308,634
Federal Income Taxes Incurred	(635,528)
Net Income	**$1,679,534**
CAPITAL AND SURPLUS ACCOUNT:	
Surplus as Regards Policyholders, December 31, 2000	$74,899,557
Net Income	1,679,534
Net Unrealized Capital Gains or (Losses)	(3,022,562)
Change in Net Deferred Income Tax	77,899
Change in Non-Admitted Assets	(119,882)
Cumulative Effect of Changes in Accounting Principle	(6,831,981)
Surplus as Regards Policyholders, December 31, 2001	**$66,682,565**

Notes to the Financial Statements

Note 1 – Cash and Short-Term Investments **$5,934,273**

Commercial paper investments of Shelter Mutual, Shelter General, and Shelter Life are commingled in a single investment account with Merrill Lynch. The total cost basis of the account was $50,421,557, as of December 31, 2001. The Company represented that $4,499,378 of the account value was attributable to Shelter General. Pooled investments are allowed pursuant to Section 379.083 RSMo (Investment Pools). However, the pooled investments must meet the requirements of this statute and a pooling agreement must be in place. Shelter General does not have a pooling agreement with Shelter Mutual or Shelter Life. The Company is directed to immediately submit a pooling agreement to the MDI for prior approval, as required by Section 379.083 RSMo, and ensure that the agreement complies with this statute.

Examination Changes

None.

General Comments and/or Recommendations

Intercompany Transactions with Shelter Mutual (page 13)

Shelter General does not have a written agreement with Shelter Mutual for the management services and facilities that are provided by Shelter Mutual and the associated costs to be allocated under the Joint Expense Allocation Agreement. The Company is directed to obtain a written agreement with Shelter Mutual, similar to the Management Services and Facilities Agreements that exist between Shelter Mutual and other subsidiaries. Such agreement should be submitted as a Form D filing to the MDI for prior approval in accordance with Section 382.195 RSMo (Transactions Within a Holding Company System).

Reinsurance Agreement with ERC (page 18)

The Company's excess reinsurance agreement with ERC, originally effective January 1, 1975, is disjointed and has confusing terminology. The 44 amendments to this agreement cannot be tied to the body of the original agreement in any coherent manner. As a result, the reinsured lines of business, the Company's retention, and the reinsurance limits are not clearly defined. It is recommended that this agreement should be restated in its entirety so that the reinsured lines of business, retentions, and limits are clearly defined.

Joint Reinsurance Agreements with Shelter Mutual (page 20)

Shelter General and Shelter Mutual have several joint reinsurance agreements. Shelter General does not directly pay reinsurance premiums to the reinsurers and does not directly receive loss recoveries. Shelter General is allocated reinsurance premiums and loss recoveries, but there is no written intercompany agreement for this arrangement. The Company is directed to obtain an intercompany agreement with Shelter Mutual for the allocation of reinsurance premiums and loss recoveries for the joint reinsurance agreements. Such agreement should be submitted as a Form D filing to the MDI for prior approval in accordance with Section 382.195 RSMo (Transactions Within a Holding Company System).

Missing Claim Files (page 21)

The Company was unable to locate three claim files and several months of research were required to locate other claim files for a statistical sample of the paid claims data supporting Schedule P of the Annual Statement. The Company appears to have numerous claim files that are either missing or improperly filed based upon the results of this sample. Section 374.205.2(2) RSMo (Examination of Insurers) requires insurers to maintain claim files for the year in which the claim is closed, plus 3 calendar years. The Company should review its procedures for the filing, maintenance, and retention of claim files and improve these procedures to ensure that all claim files are retained in accordance with the cited law.

Pooled Investments (page 26)

Commercial paper investments of Shelter Mutual, Shelter General, and Shelter Life are commingled in a single investment account with Merrill Lynch. Pooled investments are allowed pursuant to Section 379.083 RSMo (Investment Pools). However, the pooled investments must meet the requirements of this statute and a pooling agreement must be in place. Shelter General does not have a pooling agreement with Shelter Mutual or Shelter Life. The Company is directed to immediately submit a pooling agreement to the MDI for prior approval, as required by Section 379.083 RSMo, and ensure that the agreement complies with this statute.

ACKNOWLEDGMENT

The assistance and cooperation extended by the officers and the employees of Shelter General Insurance Company during the course of this examination is hereby acknowledged and appreciated. In addition to the undersigned, Shawn Hernandez, CFE, Shannon Schmoeger, CFE, Steve Koonse, CFE, Mark Nance, CFE, Andy Balas, CFE, Barbara Bartlett, and James Smith, examiners for the Missouri Department of Insurance, also participated in this examination. The firm of Expert Actuarial Services, LLC, also participated as a consulting actuary.

VERIFICATION

State of Missouri)
)
County of)

I, Tim L. Tunks, on my oath swear that to the best of my knowledge and belief the above examination report is true and accurate and is comprised of only facts appearing upon the books, records or other documents of Shelter General Insurance Company, its agents or other persons examined or as ascertained from the testimony of its officers or agents or other persons examined concerning its affairs and such conclusions and recommendations as the examiners find reasonably warranted from the facts.

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Tim L. Tunks, CPA, CFE
Examiner-In-Charge
Missouri Department of Insurance

Sworn to and subscribed before me this _______day of ________, 2003.

My commission expires: ________________ __________________________

Notary Public

SUPERVISION

The examination process has been monitored and supervised by the undersigned. The examination report and supporting workpapers have been reviewed and approved. Compliance with NAIC procedures and guidelines as contained in the Financial Condition Examiners Handbook has been confirmed.

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Frederick G. Heese, CFE, CPA
Audit Manager
Missouri Department of Insurance